

BEFORE THE STATE BOARD OF TAX APPEALS  
STATE OF ARIZONA  
100 North 15<sup>th</sup> Avenue - Suite 140  
Phoenix, Arizona 85007  
602.364.1102

1  
2  
3  
4 ORMOND BUILDERS, INC., )  
5 Appellant, ) Docket No. 1883-02-S  
6 vs. )  
7 ARIZONA DEPARTMENT OF REVENUE, ) NOTICE OF DECISION:  
8 Appellee. ) FINDINGS OF FACT AND  
9 ) CONCLUSIONS OF LAW  
10 )  
11 )  
12 )  
13 )  
14 )  
15 )  
16 )  
17 )  
18 )  
19 )  
20 )  
21 )  
22 )  
23 )  
24 )  
25 )

The State Board of Tax Appeals, having considered all evidence and arguments presented, and having taken the matter under advisement, finds and concludes as follows:

FINDINGS OF FACT

Ormond Builders, Inc. ("Appellant") is an Idaho corporation engaged in construction activities in the State of Arizona. In 1995, Appellant entered into a written contract, entitled "Construction Management Agreement," with the Payson Unified School District No. 10 ("Payson") relating to the construction of a multi-purpose educational facility and elementary school. In 1997, Appellant entered into a written contract with the Show Low Unified School District No. 10 ("Show Low") relating to the construction of a high school and gymnasium. The contracts contain the same material terms.

The Arizona Department of Revenue (the "Department") reviewed Appellant's records and determined that, based on the gross revenue from the two projects, Appellant underreported income by more than 25 percent under the prime contracting classification during the period October 1995 through February 2000 ("Audit Period"). Thereafter, the Department issued an assessment against Appellant for additional transaction privilege tax and interest under prime contracting classifications for the State of

1 Arizona and the cities of Show Low and Payson.<sup>1</sup> Appellant timely protested the Arizona and Show Low  
2 portions of the assessment to an Administrative Law Judge who denied the protest. Appellant then  
3 protested to the Director of the Department who affirmed the Administrative Law Judge's decision.  
4 Appellant now timely appeals to this Board.

5 DISCUSSION

6 The issue before the Board is whether Appellant is liable for the tax and interest assessed by the  
7 Department for the Audit Period. The presumption is that an assessment of additional . . . tax is correct.  
8 See *Arizona State Tax Comm'n v. Kieckhefer*, 67 Ariz. 102, 191 P.2d 729 (1948).

9 Appellant does not dispute the fact that its business activities generally qualify as contracting.  
10 The issue is whether Appellant was engaged in the business of prime contracting when fulfilling its  
11 responsibilities for the two projects that are the subject of this appeal.

12 A.R.S. § 42-5075 defines a "prime contractor" to mean:

13 " [A] contractor who supervises, performs or coordinates the construction, alteration,  
14 repair, addition, subtraction, improvement . . . or demolition of any building . . . or other  
15 structure . . . including the contracting, if any, with any subcontractors or specialty  
16 contractors and who is responsible for the completion of the contract. To qualify as an  
17 exempt subcontractor, a contractor must be able to demonstrate " . . . that the job was  
18 within the control of a prime contractor or contractors . . . and that the prime contractor . .  
19 . is liable for the tax on the gross income, gross proceeds of sales or gross receipts  
20 attributable to the job and from which the subcontractors or others were paid."

21 Under rule R15-5-602(C)(1) of the Arizona Administrative Code, a subcontractor is considered to be a  
22 taxable prime contractor if work is performed for and payments received from an owner-builder, owner, or  
23 lessee of real property. The Department argues that Appellant acted as the prime contractor on the two  
24 projects at issue and is liable for the tax assessed by the Department. Appellant argues that each of the  
25 trade contractors, or subcontractors, on the projects at issue is liable for the applicable tax on its portion  
of the construction.

---

<sup>1</sup> Appellant actually received a refund from Payson.

1 Appellant relies on several cases in which this Board determined that an agent of an owner-  
2 builder is not taxable based on established law that an agent is not responsible for the tax liability of his  
3 principal. See, e.g. *Mountain View Development Co. v. Arizona Dep't of Rev.*, Docket No. 442-86-S  
4 (BOTA January 1987); *Jerry's Plumbing v. Arizona Dep't of Rev.*, Docket No. 473-86-S (BOTA June  
5 1989). The Department argues that these cases do not indicate that, as a matter of law, a taxpayer may  
6 avoid tax under the prime contracting classification merely by calling itself a construction manager instead  
7 of a prime contractor and points to a more recent decision in which the Board rejected the argument from  
8 a taxpayer that it was not liable for tax because it was acting as a construction manager and agent for the  
9 property owner. *Arcon Constr. Co., Inc. v. Ariz. Dep't of Rev.*, Docket No. 1624-96-S (BOTA March  
10 1998).

11 In *Arcon*, contracts established and the taxpayer acknowledged that the taxpayer selected and  
12 contracted with all trade contractors needed to complete the construction, approved the invoices  
13 submitted by the trade contractors, and was responsible for paying the trade contractors. Only because  
14 of the taxpayer's tenuous financial situation, did the owner in that case make checks directly payable to  
15 the trade contractors. Under the contracts, the taxpayer was liable for payment. Thus, the Board  
16 rejected the taxpayer's claim that it was a construction manager and not a prime contractor. That is not  
17 the case here.

18 Appellant's contracts with Payson and Show Low were virtually the same, procuring Appellant's  
19 construction management services and describing those services as review, advice, assistance,  
20 recommendation and administration. The evidence does not show that Appellant was responsible for the  
21 completion of the project contract. For each of the projects at issue in this case, Appellant was part of a  
22 "project team" that included the owner school district, the architect and Appellant. The contracts designate  
23 Appellant as the "Construction Manager" and expressly provide that the Architect and the Construction  
24 Manager will be the Owner's *representatives* during construction and until final payment to all contractors  
25 is due. Payson and Show Low separately contracted with each trade contractor, and under the contracts,  
each trade contractor was responsible for transaction privilege tax on its particular portion of the

1 construction. Appellant did not sign any of the Payson project trade contracts and only signed alongside  
2 the owner on the Show Low project as "Construction Manager for the owner," in its capacity as the  
3 representative of the owner and not in its own individual capacity. Appellant did not sign any of the  
4 change orders, which in this case were of a significant amount. In each case, the trade contractors were  
5 responsible to the owners, not Appellant, for the completion of their trade contracts. All payments made  
6 to the individual trade contractors were "made by Appellant on behalf of the owner." Specifically, the  
7 Owner-trade contractor agreements provide that "the owner through the construction manager agrees to  
8 pay the trade contractor."

9 Appellant is just one of many subcontractors who contracted with and received payments from  
10 the owner-builder school districts on the projects at issue. Therefore, it is liable only for tax attributable to  
11 its portion of the contract.. R15-5-602(C)(1). Appellant has already paid this tax. Therefore, the Board  
12 finds that, based on the specific facts of this case, Appellant is not liable for the additional tax assessed  
13 by the Department.

14 CONCLUSIONS OF LAW

15 Appellant is not liable for the additional tax assessed by the Department. See A.R.S. § 42-5075;  
16 *Mountain View Development Co. v. Arizona Dep't of Rev.*, Docket No. 442-86-S (BOTA January 1987);  
17 *Jerry's Plumbing v. Arizona Dep't of Rev.*, Docket No. 473-86-S (BOTA June 1989). R15-5-602(C)(1).

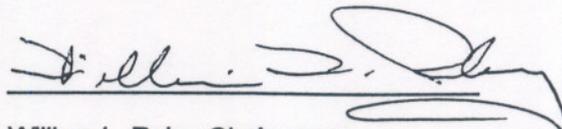
18 ORDER

19 THEREFORE, IT IS HEREBY ORDERED that the appeal is upheld, and the final order of the  
20 Department is vacated.

21 This decision becomes final upon the expiration of thirty (30) days from receipt by the taxpayer,  
22 unless either the State or taxpayer brings an action in superior court as provided in A.R.S. § 42-1254.

23 DATED this 15th day of May , 2003.

24 STATE BOARD OF TAX APPEALS

25   
William L. Raby, Chairperson

1 WLR:ALW

2 CERTIFIED

3 Copies of the foregoing  
4 Mailed or delivered to:

5 Patrick Derdenger  
6 Steptoe & Johnson LLP  
7 Collier Center  
8 201 E. Washington Street, 16<sup>th</sup> Floor  
9 Phoenix, Arizona 85004-2382

10 Lisa A. Neuville  
11 Assistant Attorney General  
12 Civil Division, Tax Section  
13 1275 West Washington Street  
14 Phoenix, Arizona 85007-1298

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25